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THE NATIONAL CITY BANK OF NEW YORK

1933

Economic Conditions
Governmental Finance
United States Securities

New York, December, 1933.

General Business Conditions

THE decline in trade and industrial operations which has been under way since July has shown signs of flattening out during November. Some of the accepted measures of business activity, including freight car loadings, electric power consumption, steel operations, and bituminous coal production, have held their ground or advanced, after allowance in the comparisons for the normal seasonal trend. This is a heartening change after four months of steady recession. It indicates that in some cases at least the necessary adjustment of over-stimulated industries to the going rate of consumption is being completed.

During the rise of prices from March to July business men covered requirements farther ahead than was believed at the time, and in fact farther than merchants themselves realized, since retail trade subsequently did not come up to expectations. The following period of dullness in the markets and decline in production was the natural sequel. A breathing space was required for the distribution of the merchandise and its absorption into consumption.

Now, with the Christmas trade at hand to accelerate the movement of goods over retail counters, there is a general hope that this period of contraction is drawing to a close. Seasonal influences will not be favorable to an upswing until after the first of year; hence there is no tendency to expect too much in the way of early upturn. But producers count upon the increased purchasing power that has been created to prevent business from dropping into the depths again, and later to provide the motive power for a Spring rise.

To be sure, experience bars the hope that new investments of private capital will contribute much toward improvement, in the present state of the bond market, and this is an important drawback. The offsetting factor is the evidence that public works expenditures are getting under way more rapidly. In other Government measures also, and in such purchases of capital goods as the industries can finance themselves or with Government aid, the possibility of increases in purchasing power is present.

Steel Operations Maintained

The steel industry has held its ground during the month, maintaining operations at 26 to 27 per cent of capacity, and Iron Age thinks it sees enough new business in sight to ensure that the rate is scraping bottom. The prospective orders include about 800,000 tons of rails, a considerable tonnage for public works, and renewed buying from the automobile factories as they get into production on new models.

Building figures make the best showing in a long time. During the first half of November, contracts awarded, as reported by the F. W. Dodge Corporation, were slightly larger than in October, contrary to the usual seasonal decline, and exceeded November of last year by 35.5 per cent. Awards in the public works and utilities classification represented nearly two-thirds of the total; they were 70 per cent greater than a year ago and about double the figures of last August. Allotments on the public works program lately have been running between $100,000,000 and $150,000,000 each week.

Residential building figures also make a good showing, running well ahead of 1932. The rising trend of material costs has caused deferred residential construction plans to be put into execution, and the improvement supports the contention of building statisticians that over the country as a whole a housing deficit has developed during the depression.

The automobile industry has been a laggard during November, due to the change-over to new models, and assemblies have been reduced to small figures. However, December will show a good increase, and January a greater one. The industry is in exceptional shape in that dealers' stocks of cars have been cleaned out by an excess of sales over production ever

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since August, and it is looking toward the first quarter with an optimism which appears to have good grounds.

Textiles and Retail Trade

The turn for the better in the textile and apparel industries waits more definitely on retail distribution than in the heavier industries, and in these lines operations have continued to decline. Reports of retail trade were better in the first half of the month, reflecting in part more seasonable weather, and also special sales at price reductions. Following the unsatisfactory retail business during September and October many stores found themselves overstocked, and marked down prices accordingly. Consumers have responded to these offerings, and department store sales in New York City have run ahead of a year ago, in dollars, for the first time since August, the increase being 2.2 per cent.

The mail order houses report a substantial improvement in their sales, the gain for Sears Roebuck & Co. in the second week of November having been 40 per cent over a year ago. These houses have been doing better than the chain stores, whose October sales were up 1.5 per cent.

In terms of the volume of merchandise moved the retail reports are still unfavorable. Retail prices on November 1 were 18.8 per cent higher than a year ago, and 25 per cent above the low point in May, according to the Fairchild index. Comparing this figure with sales, it is evident that only the mail order houses, among the chief groups of retailers, have been moving as large a volume of goods as they did in 1932. This reduced physical volume of retail trade is the most unsatisfactory feature of the situation. It is responsible for the reluctance of merchants to buy ahead at higher prices, and for the continuing recession in the textile industries and others making articles for retail distribution.

Domestic cotton consumption in October was 504,000 bales, making a satisfactory comparison with 502,000 in the same month last year. The daily average was 23,200, which compares with 29,100 at the peak in June. Silk fabric business has been light, with evidence of overstocking under the stimulus of the strike. October takings of raw silk by the mills were the smallest in many years. Demand for woolen goods has been supported by strength in raw wool prices, which in the view of the trade came just in time to overcome the danger of price cutting, due to accumulation of stocks and anxiety of mills for Spring business.

Employment Stable

Employment figures show little change. The American Federation of Labor calculates that the number of unemployed rose 11,000 during October, to 10,076,000, and accounts this a satisfactory showing, since as a rule the increase is larger. It calculates that the dollar buying power of all workers was nearly $600,000,000 a month higher than in March, and the real buying power, in terms of prices of goods bought, 23 per cent higher. This is due entirely to the increase in employment, for individual workers' wages have risen less than the cost of living, and the individual, since March, has suffered a loss of real income of 1.1 per cent.

Farm Purchasing Power

The mail order reports show that farm purchasing power is a very important factor in supporting current trade. The position of the farmer relative to other industries has changed little in recent weeks. A report of the Department of Agriculture on November 15 placed farm prices at 71 per cent of pre-war, compared with 54 a year ago, and with 49 the low point in February. In July it was 76. As compared with the low this is a good increase, and it does not represent the entire gain in farm income, since the benefit payments made to farmers for taking land out of production are not included.

The price of things bought by farmers on the same date was 117, and the ratio of prices received to prices paid was therefore 61, compared with 71 in July and 49 in February. Thus the farmer has gained relative to other consumers, as compared with the bottom of the depression, but there is still a long way to go to reach the objective of 100 per cent for this ratio, and since July ground has been lost. Hence the situation may be said to be better or worse, according to the comparison emphasized. However, there is no question as to the farmers' increased cash income and the stimulus it is giving to trade in the farm states. The Bureau of Agricultural Economics has published its estimate of gross farm income for 1933, which is $6,360,000,000, or 24 per cent more than in 1932.

Of the chief groups of farmers the cotton growers evidently are in the best position. They made their crop this year at small cost for labor, fertilizer, and insect poison; harvested the high average yield per acre of 209 pounds, which reduced costs of production; and were relieved of the usual consequences of over-production upon the price by plowing up a part of the crop, for which they were fully compensated by the Government. This has been such a favorable combination of economic factors that it will be interesting to observe its effect upon the acreage next year.

The Government's wheat acreage reduction program has been carried out with some success among those who grew wheat this year, but according to the Chicago grain statisti-

cians the reduction has been nearly offset by the replanting of Winter wheat lands which had been out of production in 1933. It is natural that owners of such lands should want to put them in wheat in 1934, to become eligible for benefit payments in subsequent years. However, comment may be deferred until official acreage figures are available.

Hog growers have been up against a snag most of the month. The processing tax went into effect November 5 at the rate of 50 cents a hundred-weight, and as packers considered it impossible to pass the tax on to consumers, in view of the competitive position of pork with other food products, they lowered their bids for hogs. This resulted in a deadlocked market for ten days or more, after which the price settled down to about $3.75 for heavyweights.

The action of the packers was dictated by the practical necessities of their business. Current prices for lard are no higher than before the processing tax was put on. It is admitted that the packing business is done on as low a margin of profit as any in this country, and there is no margin out of which the processing tax could be met. Hence it must fall upon consumers or producers, and, as the outcome shows, the consumer is the one likely to have the final say.

Trade Situation Governs Prices

It will appear from this general description of business conditions that the R. F. C. gold-buying policy, and the monetary controversy that has been aroused, have had little effect upon trade and industrial activity despite the wide fluctuations in the markets for investment capital and the foreign exchanges. A condition of monetary uncertainty is of course unfavorable for business in the long run, interfering with the making of long-term contracts, with corporate financing, and with foreign trade. However, the relation of these factors to ordinary trade is not immediate or direct, for merchants buy and sell with regard to their needs and the current state of purchasing power in their territories, rather than to monetary influences. Hence the disturbance in the capital markets has not been appreciably reflected in general business.

Conversely, commodity prices have been but little stimulated. Since the gold-buying policy was put into effect in October the average advance in a weighted list of fifteen staple commodities, represented by Moody's index number, has been less than 4 per cent. Much of this rise has been in the imported commodities, which automatically have been marked up by the depreciation of the dollar in terms of the currencies of the countries from which the commodities come.

There never was reason to think that the increased depreciation of the dollar accomplished by the gold-buying policy could effect an immediate rise in prices of domestic commodities unless it stimulated speculative buying, and the inertia of the markets indicates that business men have not wanted to buy ahead.

Cotton had a rally of more than a cent a pound during the month, and inasmuch as rising cotton prices must influence cotton goods quotations, merchandise buyers had an incentive to cover if they needed goods. However, orders showed only a moderate expansion, and the support necessary to hold the advance was lacking. Flour business has been the dullest in several years, buyers being well supplied on old contracts either carried over from last Summer or made after the October break in prices. This is the underlying cause of the reaction in wheat prices. Thus in both these important staples the trade situation, and not monetary factors, has controlled prices.

Money and Banking

The new gold buying operations of the Government have overshadowed all other developments in the financial situation. The new policies have provoked a storm of controversy, with repercussions extending into practically all markets. Instituted for the purpose of raising commodity prices, this new departure from tested monetary practice represents an experiment in price control which is regarded with satisfaction by those who believe that prices can be controlled by monetary means, and with deep apprehension by others who deny that the present low prices are due to monetary causes, and who believe that efforts to raise them by monetary means will promote further uncertainty and confusion in business and result eventually in inflation.

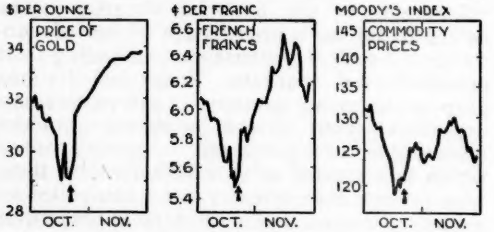
Inasmuch as the Treasury is not permitted to buy gold save at the statutory mint price of $20.67 an ounce, present operations are being carried on through the medium of the Reconstruction Finance Corporation, which pays for the gold by issuing its debentures.

On October 21, the day before the President announced the new policy, the price of gold as fixed by the Treasury was $29.01. On the 25th when the R. F. C. first began to bid for gold the price was set at $31.36, after which it was advanced by successive stages to $33.76. Actual purchases of gold have been comparatively small, amounting to only $8,500,000 of domestically mined gold, plus an undivulged amount of foreign purchases generally believed to be limited. This, however, is no handicap to the operation of the plan, since the primary object is not to acquire gold, but to depreciate the currency.

Gold at $33.76, or $13.09 above the statutory price of $20.67, is equivalent to a reduction in the gold content of the dollar of about 38 per cent. According to the terms of the monetary legislation passed by Congress this Spring, the President has authority to reduce the gold content of the dollar by as much as 50 per cent. This, in terms of gold prices, would mean $41.34 an ounce, or double the present statutory price. Nothing in the present legislation would prohibit the President from paying more than $41.34 an ounce if he wishes to do so, but such price could not become a basis for the coinage of the country without further action by Congress.

The accompanying diagram shows since October 22 the trend of the R. F. C. price for gold, the price in United States currency of French exchange representing the external value of the dollar, and Moody's price index of fifteen highly sensitive commodities, including wheat, cotton, hogs, steel scrap, sugar, wool, copper, hides, corn, rubber, silk, coffee, lead, silver and cocoa.

Prices in U. S. Currency of Gold, French Francs and 15 Commodities.
(Arrow indicates date of instituting new gold policy)



The Decline of Government Bonds

Reflecting controversy over the monetary program, Government bond prices declined sharply during the month. Both short and long maturities were affected, three and four-year Treasury notes reacting as much as 3 to 4 points, while the longer term bonds lost ground as indicated in the following table.

Decline In Representative Long-Term U. S. Government Bonds

	Oct. 21, 1933 (Close)	Nov. 22, 1933 (Low)	Points Change
Treasury 4¼s of 1947-52....	110.15	104.10	—6.5
Treasury 4s of 1944-54........	106.4	101.18	—4.18
Treasury 3¾s of 1946-56....	104.16	99.26	—4.22
Liberty 3½s of 1932-47..........	102.20	99.10	—3.10
Treasury 3⅜s of 1943-47....	102.00	98.7	—3.25
Treasury 3¼s of 1941..........	101.8	97.31	—3.9
Treasury 3⅛s of 1946-49....	100.6	94.16	—5.22
Treasury 3s of 1951-55........	98.23	93.12	—5.11
Treasury 4¼-3¼s of 1943-45	101.12	98.9	—3.3

Note: Figures after decimals represent 32nds of 1 per cent.

Accompanying lower prices and higher yields for outstanding issues, the regular weekly offerings of 90-day Treasury bills were taken at steadily advancing returns to the investor, the average basis being 0.43 per cent on November 29, against 0.15 prior to the President's gold speech.

Happily, the market steadied after the initial selling rush, and prices rallied from the low points. Realization that the decline had been too rapid, plus the announcement later that the Government intended to carry out the December financing in the usual way, without resort to currency issues, were factors in checking the decline and restoring confidence.

Money Slightly Firmer

With short-term Government issues selling on a somewhat advanced yield basis, other money rates naturally have been affected. Bankers' acceptances were twice marked up by an eighth to ⅝—½ for 60 and 90-day maturities. Stock Exchange time money was likewise a shade firmer at ¾—1¼ per cent. Call loans, on the other hand, were unaffected in price, the official quotation remaining at ¾ of 1 per cent.

Other developments in the money market were generally uneventful in character. The Federal Reserve Banks continued to taper off their purchases of Governments until in the week of November 22 the statement actually showed a slight decline of $500,000. Having built up member bank excess reserves to over $800,000,000, the Reserve Banks have been content to suspend open market operations pending the expansion of seasonal currency requirements in December, when purchases may be resumed to assist in financing the holiday retail trade.

Inflation of currency and credit continues wholly lacking. Money "in circulation"—that is, outside of the Federal Reserve Banks and Treasury—is at practically the same level as a year ago. No doubt the volume of currency actually being used in trade is larger than last year, but as the hoarding demand has diminished the total of money outstanding shows little net change. Bank deposits are but slightly higher than during the Summer, while loans and investments have failed to register any pronounced movement. Unsecured loans showed something of a seasonal rise during the Fall, but this increase was cancelled out so far as total credit was concerned by a nearly equivalent reduction in loans on securities.

Greenbacks vs. Government Bonds

A proposal frequently advanced during the depression is that the Government should pay off a substantial block of its maturing public debt in greenbacks. This proposal has been consistently resisted by the Government, but because it has a certain public following it is desirable to subject it to analysis.

The argument generally advanced in support of the proposition is that it would have

the two-fold advantage of lightening the burden of the debt, and at the same time putting purchasing power into the hands of the people with a resultant stimulus to business. It is said that both currency and bonds are Government obligations, hence there is no reason why the one should not be used to pay off the other. It is claimed that this would be a distinct advantage, for by exchanging currency for bonds the Government would save a great deal of interest.

It is true that currency and bonds are both Government obligations, but it is a mistake to assume that they are interchangeable one for the other. If it is sound monetary policy to pay off outstanding issues of the public debt with currency issues, what is the sense in putting out bond issues in the first place? Why not scrap the whole science of public finance, including the practice of levying and collecting taxes, and simply pay all Government expenses with the printing press from the beginning? Surely the answer to this question must be plain to everyone. Not even the Government has expected to get something for nothing.

It is equally a mistake to assume that the issuance of additional money in times of depression will stimulate business. It is true that during a boom, when optimism is rampant, business will absorb all the credit and currency available, and this absorption will be the means of accelerating and prolonging the boom. It is quite different, however, during a depression. At such time trade has no need for additional currency, and the public is in no mood for spending. Unless the Government should put out so much money that people would become fearful of its worth, and seek to get rid of it by exchanging it for goods having tangible value, there is no reason to believe that the issuance of the additional currency would have any effect upon prices. What would probably happen in case the Government should pay off two or three billions of its maturities in this manner would be a reinvestment of a large part of this currency in other bonds and securities. Such money as did find its way into general circulation would very likely crowd an equivalent amount of other money into retirement. Then banks, finding this money coming back over their counters, would pass it on to the Federal Reserve Banks, where it would merely add to the overflowing total of idle reserve already accumulated there.

For those of our readers who may be skeptical of this line of reasoning it is possible to cite the experience with the soldiers' bonus payments in 1931 and the issuance of national bank notes under terms of the currency amendment to the Home Loan Bank Bill in 1932. During 1931 over a billion dollars was distributed to ex-soldiers in part prepayment of adjusted compensation certificates. It was said that these payments would stimulate business. The records show that these payments neither increased the amount of money in circulation nor prevented the business situation from getting steadily worse. Again, in the Summer of 1932, Congress passed legislation authorizing national banks to issue approximately a billion dollars of additional national bank notes. Approximately $228,000,000 of these notes have been issued since this enabling legislation, yet the total volume of money in circulation has not been increased thereby. The total is about the same as it was a year ago. All that has happened is that we have more of national bank notes in our circulation and less of other kinds of money.

The Capital Market in the United States and Great Britain

In view of complaints of the alleged unwillingness of bankers to extend credit in volume sufficient to adequately finance recovery, it is pertinent to call attention to a failure in the credit supply which cannot be attributed to bankers, and which is far more serious in its effects than sporadic cases of undue caution in extending bank credit. We refer to the continued stagnation of the capital market.

In previous issues of this Letter we have repeatedly emphasized the importance of the capital market in financing the capital goods industries whose activities so largely determine the difference between prosperity and depression. Yet despite the vital role played by this market, public efforts to expand credit continue to be expended largely in the field of short-term credit, which not only has been much more freely supplied than investment credit, but serves chiefly the consumption goods industries which always hold up relatively well in bad times as well as good.

During the ten months of this year ended October 31 the volume of new capital issues, as compiled by the Commercial and Financial Chronicle, totaled only $569,000,000, exclusive of United States Government offerings and refunding issues. This is barely more than half the sum in the corresponding period of last year and the smallest for any similar period since the Chronicle began compiling the records in 1919.

Of the total of $569,000,000, approximately 65 per cent fell in the municipal classification. Corporate financing, representing the funds obtained by industry for reconstruction and promotion, fell to the extraordinarily low total of $138,000,000, compared with over $7,500,000,000 in the first ten months of 1929. The following table, comparing new issues by groups for the first ten months of each year

since 1925, indicates in striking fashion the low ebb of activity to which the capital market has been reduced.

New Capital Issues
(In Millions of Dollars)

10 Months ending Oct.	Corporate (Domestic)	Municipal	Farm Loan	Foreign	Total
1925	2,879	1,136	119	824	4,958
1926	3,190	1,142	87	949	5,368
1927	3,820	1,277	86	1,279	6,462
1928	3,804	1,067	41	1,180	6,092
1929	7,607	1,047	....	681	9,335
1930	4,183	1,174	45	980	6,382
1931	1,433	1,137	57	254	2,881
1932	304	633	59	26	1,022
1933	138	367	64	....	569

(From Commercial & Financial Chronicle. Refunding issues excluded.)

The volume of issues for refunding purposes shows a similar restriction, notwithstanding the existence of low interest rates which might be expected to encourage the replacement of high coupon bonds with low coupon issues wherever possible. According to the Chronicle, the total of corporate refunding issues during the ten months ended October was $220,000,000, the smallest for the corresponding period since 1920. In a study of refunding during the first six months of the year, R. H. Van Deusen, President of Stone & Webster, recently pointed out that of total corporate maturities of approximately $575,000,000 during that period, less than $160,000,000 were met through refunding securities sold to the public.

Public utility companies, according to this study, paid off 57.9 per cent in cash, extended or exchanged 21.3 per cent, and defaulted on 20.8 per cent. Industrial concerns paid off 27.2 per cent, extended or exchanged 38 per cent, and defaulted on 34.8 per cent. In the case of railroads, 46.3 per cent was paid in cash, 28.6 was extended or exchanged, and 25.1 per cent defaulted.

Nor has the situation as to new financing yet shown any sign of betterment. Aside from state and municipal issues, which in October ran to a somewhat larger total than in recent months, chiefly because of a sale of $29,500,000 bonds by the State of New York, the reccord of activity continues a scanty one. Corporate offerings made a particularly bad showing in October, with only $3,109,240.

This condition of inactivity in the investment market of this country is all the more noteworthy by contrast with the revival now taking place in the capital market in London. The latest circular of the Midland Bank of London contains the following table showing that new capital issues in Great Britain during the first ten months of this year were the largest in three years.

Geographical Distribution of New Capital Issues* in the United Kingdom
(In Millions of Pounds Sterling)

10 Months ending Oct.	United Kingdom	India & Ceylon	Other British Countries	Foreign Countries	Total
1925	107	3	37	19	166
1926	108	2	45	50	205
1927	139	1	57	43	240
1928	184	8	71	47	310
1929	149	10	40	36	235
1930	105	28	30	37	200
1931	36	22	14	9	81
1932	70	6	22	....	98
1933	78	5	23	8†	114

* Refunding issues excluded.
† Including Austrian Government Loan.

The feature of the table is the increase in domestic financing. Foreign issues failed to make as good a showing, partly no doubt because such offerings have been under some official restriction.

Various explanations suggest themselves to account for the marked difference in the condition in the two markets. The fear of inflation has been greater in this country than in Great Britain, and this naturally puts a damper on long-term investment. The new Federal Securities Act, aimed to throw safeguards around the issue of new securities, has turned out in practice to have certain features which have made corporations and underwriters reluctant to undertake financing of any kind. Another factor has been an impairment of the facilities for distributing securities in this country under the new banking law before the development of other facilities to take their place. It is possible that there have also been other influences. In view, however, of the importance to recovery of reestablishing an active capital market, it would seem desirable in a constructive program to take account of known obstacles and seek to remove them wherever feasible.

Debtors and Creditors

All debts, in the business sense, are payable in fixed sums of money. This is responsible for the great and general interest in the position of debtors and creditors at a time when, as during the past four years, the value of money in terms of the commodities it will buy is changing rapidly. The fall of prices, signifying that more commodities are required to discharge debts than when they were incurred, first centered attention upon the position of the debtor, and naturally any general measures for the relief of the debtor raise questions as to the interests of the creditor. In view of the widespread discussion, a statement of the facts showing who the debtors and creditors are, and in which class the majority of the people belong, may be informative.

A debtor is defined by the New Standard Dictionary as "one who is under obligation to

another, as for money or goods, or for service, benefit or help." A creditor, conversely, is "one to whom another is pecuniarily indebted." The largest and most important group of debts is that covered by the phrase "as for money," and especially the body of long-term obligations that has been created by loans of money from one person to another, or to corporations and institutions.

Every bond or similar obligation is evidence of such a loan, and is a promise to make repayment at a stated time, and to pay a fixed rate of interest until the obligation is discharged. A mortgage is an instrument of the same character. A life insurance policy is a contract calling for the payment of a stated sum to the beneficiary upon the death of the insured or the maturity of the policy, in consideration of the premium payments to the company. A bank deposit is a loan to the bank, repayable on terms agreed upon between the bank and the depositor. Banks and life insurance companies in turn make loans to governments, corporations and individuals, and thus are creditors as well as debtors.

Virtually everyone with property or savings, whether the amount is large or small, and everyone engaged in business, is either a lender or a borrower in one of the ways outlined, and hence a creditor or a debtor. Many persons are both. The four classifications described—bonds, mortgages, life insurance policies and bank deposits—represent the great bulk of the country's debts, and hence the great bulk of its credits also.

Who Are the Debtors?

It is frequently assumed that the debtor class is composed of poor people and the creditor class of rich people. However, both common knowledge and the available figures furnish proof to the contrary. In order to incur a debt a person must first of all have a credit standing. Hence the chief debtors are governments, corporations and credit institutions. Individual debtors as a rule are proprietors or property owners who borrow to carry on business or to buy and sell property. The great bulk of debt-making does not signify poverty but possession of property and activity in business.

The most extensive investigation of the debts outstanding is that made during the current year by the Twentieth Century Fund, Inc., and published in book form as "The Internal Debts of the United States" by the Macmillan Company. This is a study by a number of eminent statisticians and consultants, and their estimate is that the total long-term debt as of approximately the beginning of this year was $134,000,000,000 and the short-term business and personal debt $104,000,000,000, to which may be added $7,500,000,000 and $600,000,000 for the short-term debt of Federal and State and local Governments, respectively. These debts fall into the following classifications:

Long-Term Debts

	Million Dollars	Per Cent of Total
Farm mortgage debts	$ 8,500	6.7
Urban mortgage debts	27,554	21.7
Railroad debts	14,264	11.3
Public utility debts	11,225	8.9
Industrial debts	10,450	8.2
Financial debts	21,919	17.3
Federal debt	14,237	11.2
State and local debts	18,685	14.7
Total reported debts	$126,834	100.0
Total estimated debt	$134,280	......

Short-Term Debts

	Million Dollars
Short-term business debt	$ 89,200
Short-term personal and household debt	14,400
Short-term Federal debt	7,500
Short-term State and local Gov't debt	600
Total short-term debt	$111,700

The Federal, State and local Governments are the largest debtors, together owing $42,000,000,000. The total indebtedness given is $246,000,000,000. Of this total the portion owed by "poor people" would necessarily be confined to the personal indebtedness, a share of the farm mortgages, and a small part of the urban mortgages and business indebtedness. It is plain from the figures that the overwhelming bulk of the debts are owed by corporations or by persons falling within the rich or well-to-do income groups, and not by the poor.

Who Are the Creditors?

"If any generalizations about debtors and creditors are possible," says the study by the Twentieth Century Fund, "it is probably true that in terms of dollars the majority of debtors are corporations and the majority of creditors are individuals." The great bulk of investments represent individual savings, averaging small sums.

Of all the instruments in which individual savings in this country are invested, life insurance contracts represent by far the largest sum. The total outstanding at the end of 1932 exceeded $101,000,000,000, and the number of policy holders was about 65,000,000. These contracts include life policies, purchased both for the protection of the families of the insured or other beneficiaries and as a medium for saving; and also other contracts, such as endowment policies and annuity agreements, in which the savings feature predominates. All holders of insurance policies are creditors of the insurance company. Each beneficiary, like other creditors, will receive payment in a fixed sum in dollars. The present indebtedness of insurance companies to their policy holders (i. e., net reserves against policies, included in the foregoing table under "financial") is $17,000,000,000.

The assets held by the insurance companies against this indebtedness consist largely of promises to pay. Hence the companies themselves are creditors. Fifty-two companies owned at the end of 1932 $6,893,000,000 of mortgages and $5,990,000,000 of domestic bonds, and $6,100,000,000 of other assets. Of the long-term debt given in the table they held 22.9 per cent of the farm mortgages; 19.5 per cent of the urban mortgages; 20.8 per cent of the railroad debt and 16.3 per cent of the public utility debts; and of course substantial proportions of the other classifications.

Bank depositors are creditors in the amount of about $40,000,000,000, which is the estimated present total of all bank deposits in the country. On June 30, 1932, according to the American Bankers Association, savings and time deposits in the banks totaled $24,281,346,000. Nearly all deposits of mutual savings banks, exceeding $10,000,000,000, and a large proportion of all time deposits likewise, represent individual savings. In communities where there are no savings banks the time deposits of commercial banks are principally in the savings category. Postal savings deposits exceed $1,000,000,000.

The creditor position of the banks is represented by their loans and investments, which are the offset to their debts to depositors; and the offset to the savings deposits of course includes a large proportion of long-term bonds and mortgages. Commercial banks own bonds as part of their secondary reserve against demand deposits. Mutual savings banks alone owned at the end of 1931 $5,446,000,000 of urban mortgages, or 18.5 per cent of the total, and other banks $3,689,000,000, or 12.5 per cent. Banks owned $2,146,000,000 or 15 per cent of the railroad debts. $2,140,000,000 or 19 per cent of the utility debts, and a greater part of the Government debt than any other institutions.

More Creditors Than Debtors

As stated, the number of life insurance policy holders is about 65,000,000. The number of savings and time depositors on June 30, 1932, exceeded 44,000,000. These two main groups constitute the great bulk of the creditor class. The number of postal savings depositors exceeds 1,500,000. The individual holders of bonds, mortgages and preferred stocks total several million.

All those who depend upon pensions, charities, and trust funds invested in fixed interest obligations for their living are in the creditor position; and also those who depend upon fees and rates, since their incomes necessarily change more slowly than the cost of living. The disabled veterans, widows and dependents of veterans, and civil service pensioners of the Government are a large group falling within the creditor class. The total number receiving these payments in the fiscal year 1932 was 1,632,650. All veterans holding adjusted service certificates, numbering around 3,500,000, are creditors.

In many states and municipalities, pension systems are operated for the benefit of retired school teachers, policemen, firemen and other employees. Industrial corporations and trade unions have pension systems for retired workers, the railroads being very important in this classification. All beneficiaries of these systems, who are estimated to number more than 3,500,000, receive fixed incomes. In the case of trust funds, the nature of the investments is controlled by law, wills and indentures, and they are frequently restricted to fixed income securities.

How many individual creditors there are, after allowance for duplications, is of course impossible to say, but evidently the total must represent at least one-half of the population. The number of individuals owing long-term debts in this country probably does not exceed 15,000,000. The number of farms mortgaged is not over 3,000,000, and of individual urban dwellings in all likelihood well under 10,000,000. It is a fair assumption that the number of individual creditors exceeds the number of individual debtors in the ratio of at least four to one, and possibly five to one.

Moreover, all wage and salary-earners are in the creditor class, though not holders of time contracts. They receive pay in fixed sums, and suffer by depreciation of purchasing power as truly as by reductions in the rate of pay. Per contra, the employers of labor are debtors.

The Farm Mortgage Situation

In all discussions of debt the farm mortgage occupies a prominent place, although as shown farm mortgages represent only 6.7 per cent of the total long-term debt, and a still smaller portion of all debt. Mortgages doubled between 1910 and 1920, and showed a further increase to 1928. Since that year the total has decreased. The debt is concentrated on about 40 per cent of all farms, and represents about 40 per cent of the value of the mortgaged farms. Sixty per cent of the mortgaged farms are in Iowa, Illinois, Nebraska, Minnesota, Wisconsin, Kansas, Missouri, South and North Dakota, Indiana and Michigan.

"Even the farmer, who is looked upon as the nation's most militant debtor," says the Twentieth Century Fund's report, "is often a creditor as well—especially to the insurance company and bank. Farmers themselves also hold 14 per cent of the mortgages of, and are creditors to, other farmers." Other individuals hold 15 per cent of the farm mortgage debt, leaving about 70 per cent in the hands of institutions and other agencies.

The State of Iowa bears a larger burden of farm mortgage indebtedness than any other state. The total was $1,402,178,000 in 1928, the date of the latest complete Government figures, but has been materially reduced since. However, the people of the state had at the end of 1932 life insurance policies in the sum of $1,791,197,651, and savings deposits on June 30, 1932 totaling $256,009,000.

The farmers of Nebraska owed $599,418,000 on mortgages, and the state had $1,041,848,893 of life insurance policies and $90,034,000 of savings deposits. North Dakota owed $230,-250,000 of farm mortgages, and had $254,506,-483 of insurance policies and $40,310,000 of savings deposits. Oklahoma owed $228,513,-000 on farm mortgages and had $1,037,209,000 of insurance and $88,253,000 of savings deposits.

It is not claimed that these figures give a complete representation of the debtor-creditor relationship in those states, since other large items could be added to both sides of the account. However, it is plain that the same condition obtains there as elsewhere, and that the people are creditors as well as debtors.

Philanthropic Institutions Are Creditors

Philanthropic institutions make up a very important body of creditors. According to the publication, "Trusteeship of American Endowments," by Wood, Struthers & Co. (Macmillan, 1932) philanthropic endowment funds aggregated the following figures, classified according to use:

Property and Endowment of Philanthropic Institutions

	Million Dollars	Per Cent
Religion	$3,840	41.3
Higher Education	2,815	30.3
Hospitals	1,400	15.1
Foundations	1,000	10.7
Organized Charity	239	2.6
Total	$9,294	100.0

Of these resources, about $4,330,000,000 or 46.6 per cent was invested in domestic corporate or Government bonds, $1,330,000,000 or 14.3 per cent in real estate bonds and mortgages, and $730,000,000 or 7.8 per cent in preferred stocks, a total of $6,390,000,000 or 68.7 per cent.

It is plain from the figures that have been given that the creditor class is numerically much more important than the debtor class, and its welfare is equally essential to the welfare of the country. Long-term credit is a useful factor in business, putting into employment capital accumulated by thrift and saving. It is natural that many persons who accumulate capital are not able or do not wish to employ it actively in business themselves. Many by taste are disinclined to business pursuits, and most wage and salary earners who save prefer to invest their savings rather than to venture on enterprises of their own. Such persons lend their capital at a fixed return. On the other hand, there are others so situated that they can employ more capital than they own, and who desire to extend their operations by borrowing. Thus the opportunities to employ capital are broadened by the willingness of its owners to lend it.

Effects of Changing Price Levels

The frequently repeated statement that a higher price level will automatically make payment of debts easier is a generalization which is subject to important qualifications.

Debts are not paid out of prices, but out of profits. Whether an individual can pay his debts depends not upon his income, but upon his ability to live within the income and to have something over. Whether a corporation can meet its obligations depends not upon its gross receipts, but upon the net earnings that are left after all costs are paid.

There can be no assurance that a rise including all prices, which must necessarily increase cash expenditures as well as cash receipts, will result in an increase in net income. If the production costs of a corporation climb as rapidly as prices received, and profits are not increased, neither is the ability of the corporation to discharge its obligation enhanced. Farmers and other individual debtors may receive higher prices for their products, but if they have to pay out all the increased money income in higher prices for the things they buy they will have no more to apply against their debts, and the real burden of the indebtedness will not be lightened.

The kind of price rise that will serve the farm debtor is one that will advance farm products more than other products. This is to be sought through adjustments in farming rather than through influences affecting the general price level. The Agricultural Adjustment Act is based upon this principle.

The effects on the creditor class of a rise in the general price level are direct, inescapable, and in proportion to the rise, for when the cost of living is increased and the money income of the creditor remains fixed his purchasing power is diminished. A vast amount of the obligations held by creditors are dated before 1914, and in respect to them the creditor class has suffered by the rise in living costs ever since that date. All creditors have suffered by the losses and unemployment which have followed the collapse. Obligations in which their savings are invested are in default and in many cases already have been scaled down. If the cost of living should rise rapidly as a result of measures to relieve debtors, the purchasing power of what the creditors have left would be reduced in proportion.

The Money Question in 1873-79 and Now

We gave last month a condensed account of this country's experience with the fluctuating "greenback" currency from 1862 down to its stabilization in a fixed relation to gold in 1879. The statement was made that the conditions existing in the boom period 1868-73 and the depression years 1874-79 were practically repeated in the experience with credit inflation from 1914 to 1929 and in the disorders and depression since. We promised to give more of the details of that paper money experience, and wish to recur to the subject now.

Before doing so, however, we wish again to emphasize that the basic cause of all business depressions is a disorganization of trade relations. If every family supplied all its own wants, there would be no "business" and no possibility of a "business depression." Also, it is theoretically possible that with a system of government which determined the work every person should do and the relations which all kinds of products and services should have to each other, no confusion or disorder ever would occur. But in a society where men are free to order their own lives and bargain over their relations with each other, it is inevitable that more or less disorder shall occur. This is a condition incidental to individual liberty and social progress.

Relations are always undergoing readjustments but usually the changes are accomplished gradually and without serious disturbance, under the natural regulation of supply and demand, but occasionally a disturbance occurs of such magnitude as to unsettle the entire system. War is the most potent cause of such disturbances and a general unsettlement of credit (often related to war) ranks next in harmful influence. The two most disastrous periods of depression this country has known, the present and that of 1873-79, have been closely related to war. The last named was related not only to the fratricidal conflict within the United States, but to the Franco-German war of 1870-71. There had been no wars of such magnitude as these since the wars of the first Bonaparte, and in the meantime world industry and the use of credit had undergone great development, although nothing comparable to what followed, in the years to 1914. Not only had the world's economic system at the latter date reached a state of complexity and interdependence far beyond that of 1870, but the latest war involved more countries and was immeasurably more costly and disturbing than any before. In 1860-80 agriculture still was the occupation of most of the people, and although agriculture suffers from a depression, the people who get their living by it are less disturbed than those who live by the other industries.

To sum up, the key to every period of depression is in understanding that all business is based upon an exchange of services, which means that a disturbance of accustomed trade relations throws the entire system into confusion, with shrinking trade, diminishing employment and falling prices as inevitable results.

The Greenback Issues

We explained last month that the first greenbacks were issued to meet a great emergency in the nation's life—the emergency of civil war. The purpose was not primarily to supply more money, although it was argued that the war expenditures and demands would require more money in circulation.

There is reason to believe that if a strong central banking institution had been in existence in 1861, to handle the Treasury's borrowings and disbursements, the greenback issues would have been avoided and the country would have escaped the evils that resulted from a depreciated and unstable currency. The cost of the war was greatly increased by the depreciation, and the public debt was increased, but the most serious effects were in the instability of all business relations and the increase of private indebtedness.

The Secretary of the Treasury and leaders in Congress were impressed that it was impossible to raise money fast enough by taxation and loans to meet current expenses, swollen as they were by the war, and they resorted to what they frankly regarded as a forced loan, without interest. The currency notes were promises to pay "dollars," without in themselves specifying what a "dollar" was, and later the idea was evolved that the term did not mean anything in particular, but that the notes were simply worth whatever they would buy. The Supreme Court, however, decided that under existing law the word "dollar" meant a coined dollar of the United States. No date of payment was named, but the intent of the law was clearly indicated by the fact that the first two issues were convertible at the will of the holder into bonds which promised payment in coin at a fixed date and were to bear six per cent interest. The conversion privilege failed to prevent a substantial depreciation of the currency and the inclination was to rely upon bond issues. The authors of the original greenback legislation were not believers in fiat money or the regulation of money supplies by Congress. But they faced a great problem, and were experimenting in the use of government credit.

Depreciation of the Greenbacks

There is a limit to the amount of money which can be used at a given level of prices. That limit is reached when the working forces of the country are completely employed.

When this degree of activity has been reached, any attempt to drive the organization faster by means of more money or credit takes the form of a competitive struggle for labor and materials, which only drives up money-wages and prices, or in other words, depreciates the money. Precisely such a situation developed then and again in 1914-18, and years following, when with productive capacity fully employed, gold coming to the country by hundreds of millions and bank loans expanding, wages and the cost of living were running a race to keep up with each other. Such conditions signify inflation, not sound prosperity.

The following table shows the high, low, and average value of the paper dollar in gold in each year from 1861 to 1879:

Year	High	Average	Low	Range
1861	100.0	100.0	100.0	—
1862	99.5	88.3	74.6	24.9
1863	81.9	68.9	58.0	23.9
1864	66.0	49.2	35.1	30.9
1865	77.8	63.6	42.8	35.0
1866	80.0	71.0	59.6	20.4
1867	75.8	72.4	68.3	7.4
1868	75.7	71.6	66.7	9.0
1869	83.7	75.2	61.5*	22.1
1870	90.9	87.0	81.1	9.8
1871	92.2	89.5	86.7	5.6
1872	92.2	89.0	86.5	5.7
1873	94.2	87.9	83.9	10.3
1874	91.7	89.9	87.4	4.3
1875	89.5	87.0	85.0	4.5
1876	93.5	89.8	87.0	6.5
1877	97.6	95.4	92.7	4.9
1878	100.0	99.2	97.2	2.8
1879	100.0	100.0	100.0	—

*Decline to the low point occurred mainly in few days leading up to "Black Friday," September 24, 1869.

Source: W. C. Mitchell: "Gold, Prices, and Wages under the Greenback Standard," page 4.

These quotations show the fluctuations of the currency in relation to the British pound and other currencies on a gold basis. Such fluctuations of course affected the prices of the principal commodities exported or imported, and in this way affected internal prices and the cost of living. All prices were not affected alike. The most complete tables of wages and prices for that time are those compiled in 1891-92, under the auspices of the Finance Committee of the United States Senate and published in 1893. The work was done by the Bureau of Labor, then headed by Col. Carroll D. Wright, an eminent statistician, previously, for a long time, head of the Massachusetts Bureau of Labor Statistics. These tables employ index numbers which are percentages of the 1860 base, and give yearly averages as follows:

Year	Prices	Money Wages
1860	100.0	100.0
1861	100.6	100.8
1862	117.8	102.9
1863	148.6	110.5
1864	190.5	125.6
1865	216.8	143.1

Reviewing the two above tables it will be seen that the lowest quotations and widest fluctuations of the currency were in 1864 and 1865, but it is obvious that in all years the variations were large enough to be a troublesome factor in business calculations. This table of commodity prices and wages does not give a complete picture, since the price tables of the time were largely influenced by the export and import commodities and the wage tables by the leading trades. However, these were dominating influences.

As regards the effects of the greenback issues upon wages, Horace White's book "Money and Banking," (p. 123, 5th Ed.) says:

> The cost of living not merely followed the gold premium, but generally kept above it. The dealers in commodities advanced their prices faster and farther than gold advanced, in order thus to insure themselves against loss by rapid fluctuations.

This was the case in Germany and other European countries during the inflation which followed the latest war, and is an effect of all unstable currencies. White gives the effect of the price changes upon the value of a soldier's pay, as follows:

> Valuable lessons may be learned by considering the variations in the purchasing power of a soldier's monthly pay over commodities for each quarter of the four years of the war, as compared with the prices of January, 1860. The pay was nominally $13 per month. In the third quarter of 1862 it would buy $11.26 worth of gold and $11.11 of the commodities usually consumed in the family. One year later it would buy $9.96 gold and $8.07 commodities. One year later Congress raised the pay to $16 nominally, but even then (July, 1864) the gold value of the pay was only $6.19 and its purchasing power over commodities $6.40. In April, 1865, the gold value of the month's pay had risen to $10.77, but its value in commodities was only $7.69.

The Finance Committee report refers to the effect upon school teachers' salaries, which suffered more by the depreciation of the currency than did wages in the industries, since the latter were readjusted more rapidly. Of course, all persons in a creditor position whose dues were not readily adjustable to the fluctuations suffered in like manner.

Comparison of 1861-65 with 1914-20

It should be considered that under war conditions both prices and wages would have had an advance, even if the currency had been on the gold basis, but the fluctuations would not have been so wide. Owing to the great importations of gold and the demands for bank credit during and following the world war, an even greater inflation resulted, but wages kept pace more closely with prices. Bureau of Labor figures show that the peak for the war and post-war prices was touched in May, 1920, at 239.6 per cent of the 1913 base, while on the same base the cost of living peak in June, 1920 was 216.5 and the wage average for the year 1920 was 234. It is evident that labor fared much better in the later period, with the currency on the gold basis. The idea that the price fluctuations of either period were due to instability in gold is evidently fallacious.

They resulted from changes in the demand and supply relations of all kinds of property as offered in the markets. The war itself caused great changes in production, in wages and in trade relations; the return to peace conditions resulted in other violent changes, all with effects upon prices. It is well known that mass psychology is an important factor in all the price swings from one extreme to the other.

Post-War Reactions

The country came out of the Civil War on a very high level of prices, and owing to the lag of many incomes the popular demand at the time was for lower living costs. There was general recognition of currency and price inflation. Mr. Alexander D. Noyes in his book "Forty Years of American Finance" says:

> With flour at $16 a barrel, butter at 55 cents a pound, coal at $10 a ton, and wages and salaries advanced since 1860 hardly one-third as far as prices, the demand for currency reform obtained ready endorsement from the people.

On the strength of this sentiment the House of Representatives, on December 18, 1865, by a vote of 144 to 6 resolved as follows:

> That this House cordially concurs in the view of the Secretary of the Treasury in relation to the necessity of a contraction of the currency, with a view to as early a resumption of specie payments as the business interests of this country will permit; and we hereby pledge co-operative action to this end as speedily as practicable.

A similar situation existed in the Spring of 1920, when the Senate, on May 17th, adopted the following resolution:

> That the Federal Reserve Board be directed to advise the Senate what steps it purposes to take or to recommend to the member banks of the Federal Reserve system to meet the existing inflation of currency and consequent high prices, and what further steps it purposes to take or recommend to mobilize credits in order to move the 1920 crops.

However, the conditions which prompted the 1865 resolution already had begun to change rapidly. That was a year of violent changes; wheat averaged $1.42½ per bushel in Chicago in January and 91½ cents in December. That the war was over, further issues of paper money probably at an end and resumption contemplated, was enough to cause a substantial rise in the exchange value of the greenbacks, which of course meant lower commodity prices. Furthermore, one of the most disastrous bank panics ever known in England occurred in the Spring of 1866, and the discount rate of the Bank of England was held at 10 per cent for three months, which caused a recall of capital from the United States and disturbed confidence here. Trade slowed down, prices fell, and persons who had gone into debt under the influence of currency depreciation and rising prices began to realize the risks of their position. Sentiment began to develop in favor of more greenbacks, against ever resuming specie payments, and even for paying off the bonds in greenbacks. The resolution for contracting the currency was repealed, retirements under it having aggregated $44,000,000, which brought the total outstanding down to $356,000,000. Following the panic of 1873, the Secretary of the Treasury assumed the responsibility of re-issuing $26,000,000, raising the total to $382,000,000. This amount was subsequently reduced to $346,681,016, at which point the law was amended to require that all notes redeemed should be re-issued, and this is the outstanding amount now shown by Treasury statements.

The Business Revival

The post-war depression of 1866-67 lasted no longer than our own post-war slump of 1920-22. Notwithstanding the appreciation of the currency in gold from a low of 46.3 in 1865 to a low of 68.7 in 1868, below which it did not again fall, business revived into a five-year period of great activity.

The development of the United States had been interrupted and held back by the war, and with the war ended the energies of the people turned again to constructive enterprise. All sections of the country, but particularly the middle west, were wanting railroads. In 1850 there were only 9,000 miles of railroad in this country, and the following table shows the number under operation at intervals of five years from that date to 1900:

Railroad Mileage

1850	9,021	1880	93,262
1855	18,374	1885	128,320
1860	30,629	1890	163,397
1865	35,085	1895	180,657
1870	52,922	1900	193,346
1875	74,096		

It will be seen that while in the five years from 1855 to 1860 over 12,000 miles of new railroad were put into operation, in the next five years the construction fell to 4,456, but in the ten years from 1865 to 1875 39,000 miles were added. This tells much as to the boom period which ended in 1873. Congress had made large land grants to encourage the building of railroads through regions almost uninhabited, to open the country to settlement. With the war over, the country united, and a prospect for an appreciation of the currency, European capital was encouraged to buy American securities. Our immigration policy was wide open and the lure of cheap lands was strong. A series of short crops in Europe helped to sustain high prices for farm products and stimulated the development. No. 2 Spring wheat, which had reached the highest yearly average for war-time in 1864, at $1.48 in Chicago, and went below one dollar in 1865, rose on the short crops to an average for 1867 of $1.97 and in 1868 of $1.70, but declined to $1.12 for the year 1869 and 96 cents for 1870. These figures are based on the high and low quotations for each month.

The building of railroads resulted in the opening of farms and the building of towns and cities, all very stimulating to business in the centers, and all involving naturally much speculation in real estate and railroad stocks and a heavy increase of indebtedness.

If the post-war depression of 1866-67 corresponds to our own post-war depression of 1920-22, the period from 1868 to 1873, with its railroad construction, agricultural expansion, city building and general speculation, may be said to correspond to our own "new era" from 1925 to 1929. In both instances a war-imposed check upon development was responsible for an abnormal stimulus to post-war activities. In 1868-69 business leaped forward with demands for labor which not only gave employment to the available supply, but stimulated the largest immigration the country ever had known. From 1869 to 1873 inclusive the average number of immigrants per year was 381,000, a five year average never before approached. According to the records of the United States Bureau of Labor, wages in terms of the currency advanced 45 per cent from 1861 to 1865, but in view of the depreciation of the currency had not held their own in actual purchasing power. But from 1865 to 1872, with the purchasing power of the money rising, wage-rates also rose, reaching in 1872 a level calculated by the Bureau of Labor to be 72 per cent above the 1861 level.

Of course, the trend of property values was upward. Real estate, and stocks, as always in such periods, were largely priced on anticipations, and as usual at such times, the future was discounted too far. The credit structure was over-strained and gave way in the Fall of 1873.

The Depression of 1873-79

The period from 1873 to 1879 was one of liquidation and a readjustment of values and relations. Losses had been heavy, confidence had suffered a severe shock and time was required for recuperation and to find sure foundations for a new prosperity. Not only had credit expansion been overdone, but the anticipatory development, the opening of new lands, the construction of new facilities of many kinds, had been for the time overdone. The railroad building had been fostered for the settlement and development of the country, and the increasing production of the farm staples was having a depressing effect upon their prices. The census reports show that improved land in farms increased from 189,000,000 acres in 1870 to 284,000,000 acres in 1880, or 50 per cent, and the acreage of the principal crops kept pace.

Thus the appreciation of the currency was not the only factor in the fall of the prices of farm products in these years. It should be understood that the period from 1865 to 1900 was the greatest period for railroad building, migration and the settlement of new regions the world ever has known. Until 1880 this development was almost all in the United States, but in the eighties it spread to Canada, Australia and Argentina, besides being greatly extended in the United States. The culmination was in the nineties, when the unbalanced relation between agriculture and the other industries produced another crisis and another agitation of the money question. For the moment we are dealing with the 1873-79 situation.

The credit crisis of 1873, with the accumulation of disorders resulting from war, inflation, speculation and price fluctuations, had seriously deranged industry and trade. Unemployment was widespread, property values were falling, debtors were in distress, and under the pressure of these conditions agitation developed in favor of more experiments with paper money.

No Lack of Money

There is no evidence that the depression was caused by lack of bank credit or means of payment. The national banking system was inaugurated in 1863 and its currency took the place of the state bank notes, but the use of checks was rapidly increasing. Deposits thus became the principal medium of payments. In 1865 the aggregate of deposits and notes for all reporting banks, state and national, was $869,622,000, in 1873 it was $1,964,000,000, and in 1878 $2,221,000,000. This growth of means of payment was additional to the greenback currency, which at its highest was about $400,000,000.

Disruption of Price Relations

Reviewing that period now it appears evident that the most important factor in the depression '73-'79 was the disruption of price relations between primary products on the one hand and transportation costs and factory goods on the other. We have seen that while the currency was depreciating, wages were not keeping pace with the rise of prices. Nevertheless, wage-rates, although lagging, were constantly rising. When the currency began to appreciate, the purchasing power of the wage-earners was automatically increased, and this was helpful to trade so long as the increase was restoring the normal equilibrium between wage-rates and general prices.

However, as wages rose both in time rates and in purchasing power, and everything into which labor entered, including goods, transportation costs and taxes, was forced higher while prices of farm products were sliding down, the trade relationship became unbalanced again, this time with the farmer at the short end. He lacked the buying power to continue his purchases of other goods as before. As his purchases fell off, unemployment

appeared in all the industries, which meant a further loss of buying power, and so the vicious circle enlarged, precisely as has been witnessed under similar conditions since 1929.

Under the pressure of unemployment, and influenced presumably by declining living costs, wages declined from 1873 until in 1879 they were only 48 per cent above the 1861 level, with farm products relatively much lower. Nevertheless, in this relation the trade revival began. The explanation of recovery on this basis is that the eighteen years from 1861 to 1879 were years of great industrial progress, and the productivity of the average worker had been so much increased by the improved equipment placed in his hands that it had become possible to establish a new equilibrium more favorable to the wage-worker than the old. This is proof that the real gains of the wage-earners come by the improvements in methods of production, and that the real economic problem is that of keeping the organization in balanced relations, so that the services of all may be readily exchanged. It is a demonstration of the real solidarity of interests among all groups of the economic system.

The Disturbing Influence of Monetary Agitation

We have referred to the action of Secretary Richardson, of the Treasury, in 1874, in reissuing $26,000,000 of the greenbacks which had been retired under the act of 1865. Although this was done in the administration of President Grant, either the latter was not fully informed upon it or changed his mind about the policy, for when Congress shortly afterward passed an act directing the Secretary to reissue the remainder of the $44,000,000 retired under the act of 1865, he vetoed it in a message which took a decided stand against issuing inconvertible paper money in time of peace. He declared that it was unsound in theory and practice, saying that "if in practice the measure should fail to create the abundance of circulation expected of it, the friends of the measure, particularly those out of Congress, would clamor for such inflation as would give the expected relief."

The action of President Grant had the effect of rallying the Congress to a resumption policy, and in the same session the date for establishing the convertibility of the greenbacks at par was fixed as January 1, 1879. Previously, on March 3, 1869, the Congress of that time had passed by an overwhelming vote what was known as the Public Credit Act, definitely affirming that the Government's bonds were payable in coin, and concluding with the declaration that the United States "solemnly pledges its faith to make provision at the earliest practicable period, for the redemption of the United States notes in coin."

Notwithstanding these declarations and the passage of the redemption act, which might be expected to allay misgivings about the Government's policies and thus afford a basis for confidence and enterprise, agitation for the repeal of the resumption act and for new issues of greenbacks was active and exerted a disturbing influence. It lessened the amount of capital available for loans, increased interest rates, made renewals or extensions more difficult, increased the pressure for the liquidation of obligations, affected all property values, involved all business in uncertainty, and discouraged enterprise.

The Argument for Sound Money

The supporters of the resumption policy laid emphasis first of all upon the maintenance of the national honor, which in their belief required faithful discharge of the obligations written in the Government bonds and on the face of the greenbacks. These obligations had been accepted by the public and the pledges had been reaffirmed repeatedly by acts of Congress, to secure the benefit of lower interest rates in refunding operations. The plea that the value of the money had changed was answered by saying that the price-changes and disorders incidental to the war and the policies of the Government were unavoidable conditions of carrying on the war; that it was impossible to review and readjust the effects of such changes as between individuals; the Government could be right only by maintaining a consistent public policy.

Supplementing this, they urged that the only way to restore confidence and prosperity was by reestablishing the country's monetary system upon a firm basis, having definite relations to the monetary systems of the other important countries, and by scrupulously observing its own obligations. If the Government should adhere to these policies, they were assured that the people, acting with the enterprise and resourcefulness they had ever displayed, would achieve prosperity.

Prosperity in the Eighties

There can be no question about the business revival which followed the restoration of the currency to the gold basis on January 1, 1879. Business quickly felt solid ground under its feet. The money question was considered as settled. Home capital flowed freely into investments and foreign capital came in to participate in the development of the country. The pressure upon debtors was relieved. Interest rates underwent a pronounced decline. Property values increased. Employment recovered, readily absorbing a heavy immigration. The prices of farm products improved for several years, although later the expansion of farm acreage as the result of railroad build-

ing in new regions again became a depressing influence. The decade of the eighties was one of great industrial development, which was reducing production costs, although wages were rising. Railroad charges upon all classes of freight between Chicago and New York were reduced about one-half between 1860 and 1890, and the average ton-mile charge for the country in about the same proportion. Ocean freight charges were reduced in like manner. All manufactured goods were declining as a result of increased efficiency in production, and the standard of living for the entire population was rising in consequence.

The figures compiled by Labor Commissioner Wright for the Senate Finance Committee in the early nineties showed that in 21 groups of leading industries, including the railroads, the construction trades, the textiles, metals and other leading lines, the average increase of wages in the 31 years from 1860 to 1891 was 60.7 per cent, or at the average rate of nearly 2 per cent per year. The report included a calculation of living costs, which reached the conclusion that for corresponding standards these had undergone a reduction in the same time of between 4 and 5 per cent. In a price table including 223 commodities, only two groups showed increases, these being food and lumber and building materials. On the average of all the prices, these 223 commodities showed a decrease in the 31 years of 7.8 per cent. These figures in connection with the rise of 60 per cent in wages attest the gain in general welfare during this period, and the effective recovery from the disorders of the seventies.

This showing for 31 years from one gold standard price level to another, notwithstanding the disturbances of the intervening period, for which the gold standard was in no way responsible, leaves little basis for an argument in behalf of a "managed" commodity standard. Assuming a debt running over that period to have been paid in a currency adjustable to the change in prices, instead of in a currency having a fixed relation to gold, the saving to the debtor would have been 7.8 per cent, or about ¼ of 1 per cent per year over the period. On the other hand, the factors in production had the gain from the increased productivity of the industries, which in the case of the wage-earners was 60 per cent. The wage-earners were the chief beneficiaries of the period, for they gained both in wages as stated and in the purchasing power of a given wage.

1860-79 and 1914-33

The conditions affecting business in these two periods were so much alike that a study of them is instructive. War and inflation were the original influences; rising prices, speculative booms and an abnormal growth of indebtedness were resulting features. This country did not issue irredeemable paper currency during the last war or the boom period which followed, but the inflation of bank credit as currency was relatively greater than the greenback inflation of the sixties, and could not have occurred but for the war. The derangements in industry and trade directly and indirectly resulting from the last war were vastly more important than those resulting from the war of 1861-65. The expansion of agriculture from 1914 to 1932 was very similar to that from 1865 to 1879, and the loss of purchasing power to agriculture had similar effects in both instances. The money question is practically the same now as then, that of maintaining the long established monetary standard, which has not been responsible for the price disturbance of either period.

The plea now made that prices cannot rise, and that prosperity cannot be regained, without depreciating the money, is practically unchanged from that which was made in the seventies and which was completely disproved by the prosperity of the eighties.

As stated at the beginning of this article, the cause of all business depressions is disorder in trade relations, which interrupts or slows down the normal flow of trade and thus creates the surpluses which depress prices. To illustrate, there are right relations between wheat, corn, cotton, dairy products, live stock, etc., and manufactured goods, transportation and taxes, which must be maintained in order to have prosperity. This just equation was disturbed in the seventies and is disturbed now.

The Department of Agriculture is convinced that the trade relations between agriculture and the other industries are badly out of balance and acting on the above reasoning has adopted an extensive policy to correct them.

Since there is room to believe that credit resources and means of payment already are ample to sustain a price level as high as that of 1926, it follows that if trade relations were adjusted business would readily revive and prices rise to that level without any change in the monetary system. On the other hand, if the Department of Agriculture is right in its analysis of the situation and its policy of curtailing production is successful in restoring balanced relations, it follows that devaluation of money is unneeded, and if also resorted to would carry the price level far beyond the 1926 level which is named as the level required for just relations between prices and debts. This is the danger of inflation which arouses apprehensions. If provision is made for great additions of currency or bank credit, without allowing for the resources now lying unused, return to a normal state of confidence and business conditions will upset the calculations upon which action has been based.

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